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ABSTRACT

A study was conducted to assess the extent to which (1) stockholders consider corporate annual reports to be informative and useful, (2) they actually read annual reports, (3) they consider annual reports to be impressive, and (4) they are motivated by the annual report to invest further in corporations in which they already own stock. After the questionnaire was designed, reviewed, and pilot tested, it was sent to 1,120 stockholders (80 stockholders for each of 14 companies); 549 returned a usable questionnaire. Then the data were analyzed. The major findings of this study are that the reactions of stockholders to corporate annual reports are generally favorable; that stockholders regard annual reports as generally informative, effective, successful, honest, open, impressive, and useful; that stockholders think the annual reports are too long, but they believe that the reports inform the reader of the financial condition of the corporation reasonably well; that the annual reports stimulate stockholders to invest; that 9 out of 10 stockholders spend at least some time examining the report; that most of the stockholders have attended college and are over 56 years old; and that stockholders react favorably to the reports regardless of age, sex, or level of education, but the time spent reading the report increases as the age of the stockholder increases. (EL)

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STOCKHOLDER REACTIONS TO CORPORATE ANNUAL REPORTS

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ABSTRACT

Stockholders are considered to be the most important recipients of corporate annual reports. But what are their reactions to these reports? This study answered that question. Findings led to the conclusion that stockholder reactions to corporate annual reports are generally favorable.

INTRODUCTION

Research by Neilson and Lind led to the conclusion that corporate executives believe stockholders are a most important element in the financial security of a corporation (Neilson and Lind, 1977, p. 34). Executives also consider stockholders to be the most important recipients of the corporate annual report ("Management Looks at Financial Reports," 1973, p. 92).

Also, researchers have concluded that a major portion of the solution to better relations between the stockholder and the corporation is improved communication. The corporate annual report, in the researchers' opinion, is one medium through which communication can be improved (Neilson & Lind, 1977, p. 10).

OBJECTIVES OF THE STUDY

The purpose of this study was to assess stockholder reactions to corporate annual reports and to ascertain the extent to which selected objectives of these reports were met. The study was designed also to indicate (1) the extent to which stockholders consider annual reports to be informative, (2) the extent to which stockholders consider reports to be useful, (3) the extent to which stockholders actually read annual reports, (4) the extent to which stockholders consider corporate annual reports to be impressive, and (5) the extent to which stockholders are motivated by the annual report to invest further in corporations in which they already own stock.

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PROCEDURE FOR OBTAINING STOCKHOLDER REACTIONS

Stockholder reactions to corporate annual reports were obtained by the following three-step procedure:

1. Identify corporations that would participate in the study;
2. Design a questionnaire to measure stockholder reactions to corporate annual reports;
3. Mail questionnaires to stockholders.

Identifying Participating Corporations

The study was delimited to Fortune 500 corporations of 1977. These corporations were selected on the assumption that the size of a corporation and its attempts to achieve effective communication with stockholders are directly related. Smith and Smith (1971, p. 555) as well as Pashalian and Crissy (1950, p. 245) made similar assumptions in their research studies.

The basis on which invitations to participate in the study were issued was the "1977 Percentage of Total Return to Investors" (the percentage derived by dividing the dividends paid in 1977 plus the price appreciation of a share in 1977 by the cost of that share at the beginning of 1977). If a corporation had a 10 percent or greater increase in its "1977 Percentage of Total Return to Investors," it was invited to participate in the study. One hundred eighteen members of the Fortune 500 for 1977 had a 10 percent or greater increase in their "1977 Percentage of Total Return to Investors" and were invited to participate in the study. Six of these corporations agreed to participate in the study.

If a corporation had a 10 percent or greater decrease in its "1977 Percentage of Total Return to Investors," it too was invited to participate in the study. One hundred thirty-five members of the 1977 Fortune 500 had a 10 percent or greater decrease in their "1977 Percentage of Total Return to Investors." Eight of these corporations accepted the invitation to participate in the study.

Of the 14 corporations which did participate, three ranked in the first 100 of the Fortune 500; one, in the second 100; four, in the third 100; five, in the fourth 100; and one, in the fifth 100. Each participating corporation was requested to select 80 stockholders for participation in the proposed study. Questionnaires were sent to a total of 1,120 stockholders--549 returned a usable questionnaire. Some corporations sent the questionaire with their own cover letters. Other corporations sent their 80 stockholders the questionnaires themselves but used the researcher's cover letter. Still other corporations sent a list of the names and addresses of their 80 stockholders to the

researcher who mailed the questionnaires and cover letters to the stockholders.

Developing the Questionnaire

The study was designed in part to identify the two chief corporate objectives of the annual reports prepared by participating corporations. Executives were therefore asked to identify the objectives of their respective annual reports and to send the researcher a list of these objectives.

The two objectives of corporate annual reports named most frequently by executives of participating corporations were

1. to reveal the basic financial condition of their corporations and

2. to attract new or additional investment in their corporations.

After these objectives had been identified, the questionnaire was developed.

The inquiry technique used in the questionnaire is the semantic differential. This technique was selected because of its ability to measure attitudes. The three central concepts around which the questionnaire was developed are

1. stockholder reactions to the corporate annual report in general,

2. stockholder reactions to the financial section of the report, and

3. indication of the probability of additional investment motivated by the annual report.

The pairs of polar adjectives which were possible descriptors of annual reports were selected for inclusion on the questionnaire by means of a word-by-word analysis of The Word Book, which contains 40,000 words. Adjectives which could be meaningful descriptors of corporate annual reports were identified in the analysis and placed on a list. The adjectives selected were arranged in polar pairs for use in the questionnaire.

The questionnaire was then arranged in two major sections. The first section of the questionnaire was designed to gather general data about the stockholder (e.g., age, sex, formal education, etc.), the time spent by the stockholder in reading or skimming the annual report, and the stockholder's intensity or recall of the content of the annual report.

The second section of the questionnaire was divided into three subsections. The first subsection was designed to measure stockholder reactions to the annual report in general. The second subsection requested stockholder reactions to the financial section of the specific annual report. The last subsection, entitled "Other Reaction," was

designed to measure the report's ability to attract additional investment from present stockholders.

In its initial form, the questionnaire was reviewed by members of the researcher's advisory committee and by the executives of 12 of the participating corporations. Committee members and executives were asked to evaluate the questionnaire. Several changes in the questionnaire resulted from these evaluations.

The questionnaire was then pilot tested. In the pilot test, 40 questionnaires were sent to stockholders of five different corporations. Seventeen of the questionnaires were returned. The main purpose of the pilot study was to identify problems respondents might have in understanding and reacting to the items on the questionnaire. One change in the questionnaire--a clarification of language--was made as a result of the pilot study.

Distribution of the Questionnaire

On February 1, 1979, packages containing the questionnaires and stamped, self-addressed envelopes were sent to corporations which provided their own cover letters and which had agreed to mail the questionnaire themselves. On the same day, similar packages were sent to corporations for which the researcher provided the cover letter. Both of these groups were instructed to mail the questionnaire to stockholders on February 15 or 16.

Individual cover letters were prepared for stockholders for whom names and addresses had been provided. On February 16, 1979, the cover letter, a questionnaire, and a stamped, self-addressed envelope were sent to each of these stockholders.

On March 8, 1979, a follow-up letter and a questionnaire were mailed to all stockholders whose questionnaires were sent to them by the participating corporations. The stockholders were asked to complete and return the questionnaire if they had not already done so. Also on March 8, 1979, those stockholders that had not responded to the initial cover letters and questionnaires mailed by the researcher were sent follow-up letters and questionnaires.

All of the corporations that mailed their annual reports after February 28, 1979, elected to mail the questionnaire themselves but used the researcher's cover letter. On February 1, 1979, packages containing the cover letters, the questionnaires, and the stamped, self-addressed envelopes were sent to these corporations. They were asked to mail the initial questionnaires to their selected stockholders on April 2, 1979. Follow-up letters and questionnaires were mailed on April 20, 1979.

DATA ANALYSIS

It is conceivable that attitudes toward corporate annual reports may be influenced by the financial performance of the corporations.

Therefore, the reactions of stockholders to corporate annual reports could be the result of a corporation's performance rather than the impact of the report itself. To determine whether the data obtained in the questionnaires were contaminated by the financial performance of a participating corporation, financial performance was evaluated six ways: (a) 1978 Percentage of Total Return to Investors, (b) 1968-78 Percentage of Total Return to Investors, (c) 1977 Percentage of Total Return to Investors, (d) 1967-77 Percentage of Total Return to Investors, (e) 1968-78 Growth Rate of Earnings per Share, and (f) 1967-77 Growth Rate of Earnings per Share. In each of these ways, the financial performance of each participating corporation was classified as strong, weak, or neither.

The basic criterion used to determine these classifications was the average inflation rate for the time period expressed in the title of the method of evaluation. For example, for "way e," 1968-78 Growth Rate of Earnings per Share, the criterion used for classification of the corporations was the average inflation rate for the period 1968-78.

For a corporation to be classified as strong, its percentage of total return to investors or its growth rate of earnings per share had to exceed the average inflation rate of its designated time period. For a corporation to be classified as weak, its percentage of return to investors or its growth rate of earnings per share had to be zero or negative. For a corporation to be classified as neither, its percentage of total return to investors or its growth rate of earnings per share had to be above zero and not exceed the average inflation rate of its designated time period. Three corporations were excluded in the analysis of data in order to achieve proper contrast between strong and weak corporations.

The statistical procedure known as the median test was employed to determine whether significant differences existed between stockholder reactions of strong corporations and stockholder reactions of weak corporations.[1] This test provides information about the likelihood that two independent groups have been drawn from populations with the same median.

Eight pairs of polar adjectives were used as the bases for these median tests. In each test, the reactions of the stockholders of strong corporations were compared with the reactions of the stockholders of weak corporations.

In a check for questionnaire reliability, the reactions of stockholders on the initial questionnaire were compared with the reactions of stockholders on the follow-up questionnaire. This comparison was made in order to check the reliability of the questionnaire. Median tests were used to identify whether significant differences existed

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[1]For any difference or relationship to be considered significant in this study, at least the 0.05 level of significance was required.

between stockholder reactions to the initial questionnaire and stockholder reactions to the follow-up questionnaire.

The annual reports used in this study were either the 1977 or 1978 annual reports of participating corporations. The dates on which these annual reports were mailed were divided into three categories: (a) prior to August 1, 1978; (b) between August 1, 1978, and February 28, 1979; and (c) after February 28, 1979. As another check on questionnaire reliability, a comparison was made of stockholder reactions to the reports mailed during the three different time periods. Median tests were calculated to determine whether significant differences existed between stockholder reactions to the annual reports mailed during these time periods.

Percentages and median responses were used to identify characteristics of stockholders who participated in the study. Median responses were used as the measure of central tendency in this study because of the nature of the distribution of stockholder responses.

Median tests were calculated to determine whether significant differences existed between the reactions of male stockholders to annual reports and the reactions of female stockholders to annual reports. If statistically significant differences were revealed by the median tests, the raw-score responses of the two groups were compared to ascertain to what extent the differences were meaningful.

FINDINGS

The major findings of this study are summarized in the following categories: (1) stockholder reactions to corporate annual reports, (2) the extent to which selected corporate objectives of annual reports are achieved, (3) characteristics of stockholders, (4) checks for contamination of data and for reliability of the questionnaire, and (5) analyses of stockholder reactions by sex, by age grouping, and by level of education.

Stockholder Reactions to Corporate Annual Reports

Stockholder reactions to corporate annual reports were identified by using the median response to the pairs of polar adjectives on the questionnaire. The average number of responses to all pairs of polar adjectives was 322.

The reactions of the stockholders to corporate annual reports were generally favorable. Stockholders indicated that they felt corporate annual reports were "quite thorough," "quite honest," and "quite successful." They felt that annual reports were effective and justified. Stockholders also described annual reports as interesting, attractive, and readable. They indicated that annual reports were "quite welcomed."

The extent to which annual reports were considered useful or valuable was measured by asking stockholders to react to the pair of polar adjectives "useful/useless." Their responses indicated that they regard the reports as "quite useful." Stockholders were asked to respond to the pair of polar adjectives "informative/meaningless" to indicate how informative they considered annual reports to be. Stockholder responses indicated that annual reports were considered "quite informative."

The pair of polar adjectives "impressive/worthless" was used to describe the extent to which stockholders were favorably impressed, in a general way, by the annual reports. Responses indicated that stockholders were "somewhat impressed" by the annual reports which they received. Three other stockholder reactions which suggested less stockholder satisfaction with corporate annual reports indicated that stockholders regarded annual reports as only "somewhat simple," "somewhat panoramic," and "somewhat realistic."

The response which displayed the most negative stockholder reaction was the reaction to the pair of polar adjectives "brief/long." Stockholders indicated that they regarded annual reports as "somewhat long."

The Extent to Which Selected Objectives of Annual Reports Are Achieved

The two objectives of corporate annual reports expressed most often by executives of participating corporations were (1) to inform the reader of the corporation's financial condition and (2) to attract new or additional investment in the corporation.

Stockholders were asked to react to six pairs of polar adjectives on the questionnaire to ascertain the extent to which they believed they were informed by the annual report about the financial condition of their respective corporations. Stockholders reacted favorably to the financial sections of the annual reports. They described the financial sections as "quite factual," "quite good," and "quite informative." They indicated that the financial sections were "quite needed" and "quite complete." Stockholders indicated, however, that the financial sections of annual reports were only "somewhat simple."

To measure the extent to which stockholders were motivated by the annual reports to make additional investments in their respective corporations, stockholders were asked to react to the pair of polar adjectives "encouraged/discouraged." The median response of stockholders was favorable. Stockholders indicated that they were "quite encouraged" by the annual report to invest additional funds in their respective corporations.

Characteristics of Stockholders

Information about the characteristics of stockholders was derived from stockholder responses to the questions on the initial part of the questionnaire.

To ascertain the degree to which corporate annual reports are actually read, stockholders were asked (a) how thoroughly they read the annual reports and (b) how much time--if any--they spend reading or skimming the annual report.

Approximately 46 percent of the stockholders indicated that they had read or skimmed all or part of the annual report. Approximately 15 percent indicated that they had read all the report. About 15 percent of the stockholders spent over 30 minutes reading or skimming the annual report. Over 45 percent of the stockholders indicated that they spent over 15 minutes reading or skimming the annual report. Just under 10 percent indicated that they had not read or skimmed any of the annual report.

Other findings on the characteristics of stockholders were as follows:

1. Stockholders, regardless of the number of corporations in which they own stock, generally spend 6 to 15 minutes reading or skimming an annual report.

2. Just over 73 percent of the stockholders had attended college, had graduated from college, or had earned a graduate degree.

3. Slightly over 61 percent of the stockholders were 56 years of age or older; just over 34 percent of the stockholders were over 65 years of age.

4. Male stockholders who responded to the questionnaire outnumbered female respondents almost 3 to 1.

Check for Contamination of Data and for Reliability of the Questionnaire

In the check for data contamination, 48 median tests were calculated to compare stockholder reactions to annual reports of strong corporations and stockholder reactions to annual reports of weak corporations. Ten of these tests revealed significant differences between the two groups. However, median raw-score responses for both groups in nine of these tests were either identical or very similar. Thus, the analysis of data disclosed little evidence of meaningful contamination.

In the two checks on the reliability of the questionnaire, only one of 36 median tests indicated a significant difference between the two groups compared. The median raw-score responses of the two groups, however, were very similar. These two checks indicated that the questionnaire was reliable in collecting the data of the study.

Analyses of Stockholder Reactions by Sex, by Age Grouping, and by Level of Education

Thirty-three median tests were calculated to compare the reactions of male stockholders to annual reports with the reactions of female stockholders to annual reports. The results of these tests indicated no meaningful differences between reactions of male stockholders and those of female stockholders.

Analysis of variance was used to compare stockholders reactions to annual reports by age groupings. Of the nine analyses which revealed significant differences, only one appeared to be meaningful. A significant difference existed between the age groups in the amount of time spent reading or skimming the annual report. A direct relationship existed between the amount of time a stockholder spent reading or skimming the annual report and the age of the stockholder--the older the stockholder, the more time the stockholder spent reading or skimming the annual report.

Analysis of variance was used to identify significant differences between the reactions of stockholders by the level of their education. Of the 32 analyses made, 8 revealed statistically significant differences. An examination of these differences disclosed that in no instance was a difference meaningful.

CONCLUSIONS

Based on the findings of this study, the following conclusions were drawn:

1. For the populations with which this study is concerned, stockholders are generally pleased with the annual reports of their respective corporations.

2. Annual reports are regarded by stockholders as generally informative, effective, and successful. They are also viewed as interesting, readable, attractive, and thorough.

3. Stockholders believe annual reports are honest and open, and they welcome them to their homes or offices.

4. For the most part, stockholders consider annual reports to be both impressive and useful; however, they also regard them as somewhat complex.

5. The characteristic of annual reports to which stockholders expressed the strongest negative feeling was the length of annual reports. Stockholders consider annual reports to be "somewhat long."

6. Stockholders believe that corporate annual reports perform reasonably well in their efforts to inform the reader of the financial condition of the corporation. However, they consider the financial section of the annual report to be overly complex.

7. Corporate annual reports apparently serve to stimulate stockholders to invest in those corporations in which stockholders already own stock.

8. Nine out of ten stockholders spend at least some time examining the annual report. About 45 percent of the stockholders spend over 15 minutes reading or skimming the reports which they receive. A small group of stockholders--just under 10 percent--do not spend any time reviewing their annual reports; however, about one in six stockholders reads the complete annual report.

9. About three of every four stockholders have attended college, have graduated from college, or have received a graduate degree.

10. One in every three stockholders is over the age 65; six of every ten are over 56 years of age.

11. Stockholders react similarly to corporate annual reports regardless of their sex, age, or level of education. However, the time spent reading an annual report increases as the age of the stockholder increases.

RECOMMENDATIONS

As the result of the findings and conclusions resulting from this study, the following recommendations are made:

1. Since stockholders react favorably to corporate annual reports, regard these as interesting and informative, and are influenced to make additional investments in their respective corporations, the use of corporate annual reports should be continued.

2. Corporations which distribute annual reports should give special attention to the length and complexity of their reports. Although these aspects of the annual report were not severely criticized by stockholders, stockholders indicated that improvement is needed.

3. Additional research is needed to measure specifically what causes stockholders to regard complexity as one of the least favorable aspects of annual reports.

4. Research should be conducted to identify what specific changes stockholders would like to see made in corporate annual reports.

5. Research is needed to ascertain the kinds of corporate communications--i.e., annual reports, quarterly reports, newsletters, progress summaries, special announcements, etc.--that stockholders would like to receive from corporations in which they own stock.

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